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An Emerging Health Insurance Option Primarily for Small Business — Individual Coverage HRA

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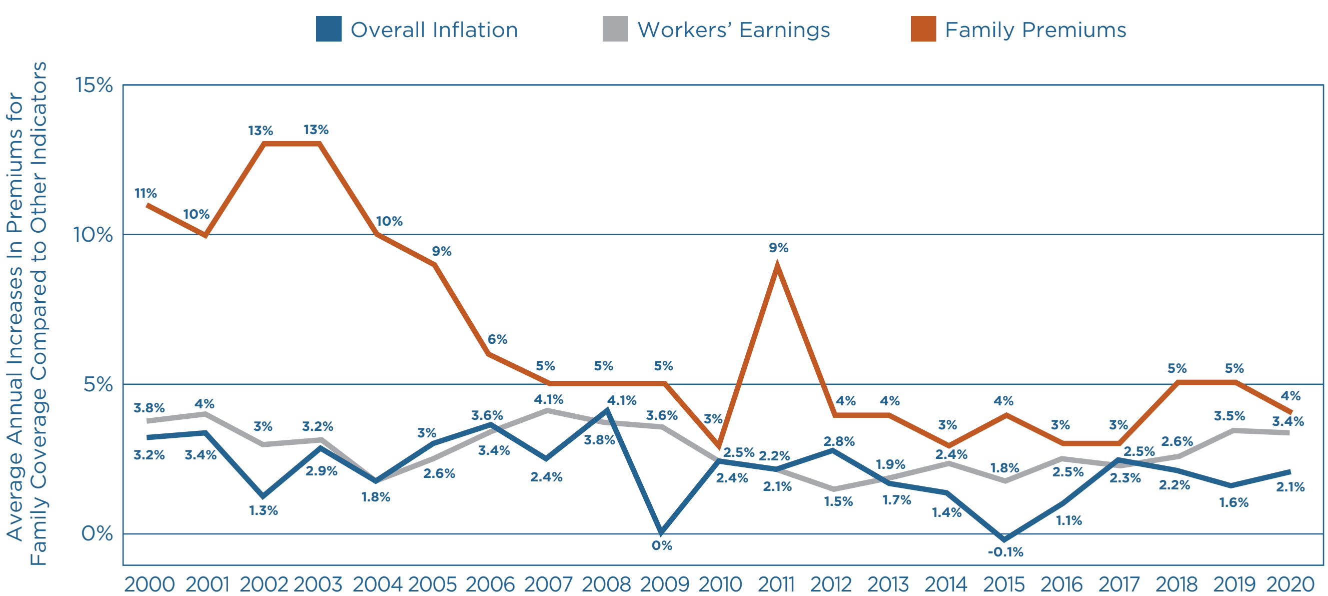
Health insurance ranks as the top benefit employees seek from their employers due to the cost of health insurance coverage and the fact that most large employers provide health insurance to their full-time workers. Yet in Michigan in 2019, only 29.3% of small private sector employers with fewer than 50 employees offered company-sponsored health insurance to their employees. Comparatively, 96.8% of Michigan private sector large employers with 50 or more employees offered company-sponsored health insurance to their employees.[1] This results in small private-sector businesses having a significant competitive challenge relative to larger employees in the attraction and retention of employee talent. The high cost of health insurance premiums is the main reason why small businesses forgo this critical benefit for their workers. The COVID-19 pandemic has had a devastating financial impact on small businesses, particularly those in the retail, restaurant and hospitality industries, and as the economy reopens, it will be tougher than ever for small businesses to sponsor health insurance coverage for their employees as they struggle for economic survival.

Since 1998, The Kaiser Family Foundation has conducted an annual employer health benefits survey to assess key health insurance trends affecting employers and their covered employees. Kaiser's annual survey is recognized in the employee benefits industry as a preeminent source for measuring employer health insurance trends and the annual increases in health insurance premiums paid by employers and their employees. For the 2020 survey, Kaiser surveyed 1,765 randomly selected, non-federal, public and private employers with three or more workers, in partnership with the University of Chicago.[2] Each year the survey reports the average cost of single and family health insurance coverage. For small employers, with fewer than 50 employees, the 2020 average annual single-coverage premium was $7,483 and $20,438 for family coverage. Over the past five years, average family coverage premiums have risen 22%, with increases of 55% over the past 10 years.[3] **Exhibit 1** shows how annual family health insurance premium increases have outpaced both workers' earnings and overall inflation by a wide margin from 2000 to 2020. The consistent year-over-year increases in health insurance premiums relative to annual inflation and workers' wage increases make employer-sponsored coverage affordability challenging for businesses of all sizes, but daunting for small businesses that often lack the financial resources of larger entities.

Exhibit 1: Annual Health Insurance Premium Increases Have Exceeded Workers' Earning and Inflation by Wide Margin 2000-2020



Source: Kaiser Family Foundation Health Benefits Survey, 2018-2020; Kaiser/HRET Survey of Employer-Sponsored Health Benefits, 2010-2017

[1] Percent of Private Sector Establishments That Offer Health Insurance to Employees, by Firm Size, Kaiser Family Foundation, 2019; Kff.org.
[2] Kaiser Family Foundation 2020 Employer Health Benefits Survey, October 8, 2020; Kff.org.
[3] Ibid

An option to help small businesses fund employee health insurance premiums

Recognizing that small businesses struggle to afford sponsoring health insurance coverage for their employees, the Trump Administration, on October 12, 2017, issued Executive Order 13813, authorizing the Departments of the Treasury, Health and Human Services and Labor to expand the usability of health reimbursement arrangements to help small businesses fund health insurance coverage for employees.[4] The new rules creating the Individual Coverage Health Reimbursement Arrangement (ICHRA) were issued in June 2019, with a start date of January 2020.

Table 1 provides a summary of how the ICHRA differs from employer-sponsored health insurance coverage. ICHRAs initially will have the greatest appeal to small employers that currently do not offer health insurance coverage for eligible employees. However, ICHRAs may be used by employers of all sizes, and it is anticipated by some health insurance industry experts that certain large employers may find ICHRAs ideal for their employee populations due to the unique ICHRA structure and the insurance premium funding flexibility the ICHRA provides to employers.

Table 1: Comparing the ICHRA to traditional health insurance plans

ICHRA	Traditional group health plan
• **Employer determines how much to pay toward health insurance premiums through an ICHRA.** Employer determines how much to pay for single and family coverage. Eligible employees purchase individual health insurance coverage and receive the premium reimbursement from the ICHRA. Employer does not sponsor health insurance coverage. The employer controls the ICHRA and determines eligibility for ICHRA reimbursement.	• **Employer is responsible for funding most of the health insurance premium for covered employees.** Employer has less budget control over funding health insurance premiums due to rising annual premiums and minimum employer premium requirements. Smaller employers often struggle to provide minimum required premium payments for sponsored group coverage.
• **More plan choices for employees** as coverage is purchased in the individual insurance market, with multiple guaranteed issue health insurance options offered by a variety of health insurance carriers in the state of Michigan and in national markets for out-of-state employees.	• **Limited plan choices for employees** typically through one health insurance carrier that the employer selects. Selected coverage may be cost prohibitive for some employees based on the amount of required employee premium contributions for coverage in the health plan.
• Employer is the "financier" of health premiums and permits employees to select individual market coverage that meets their health and budget requirements. Higher rates of reimbursement can be established for older employees who pay more for coverage than younger employees. In addition, reimbursement can vary based on classification of employees such as full-time versus part-time employees, or single versus family coverage.	• Employer is the "sponsor" of coverage and is responsible for following the numerous requirements associated with plan sponsorship, including paying for premiums, eligibility, enrollment and termination of coverage. Employers with 20 or more employees are required to provide COBRA continuation coverage for terminated employees and their dependents.
• Health insurance **coverage continues** when the employee fails to meet eligibility requirements or terminates employment. If the employee continues paying premiums, coverage will remain in effect as insurance coverage is purchased from the insurance carrier by the employee.	• Health insurance **coverage ends** when the employee fails to meet eligibility requirements or terminates employment, with COBRA coverage possible for a limited number of months following loss of coverage. COBRA coverage is often cost prohibitive for the employee to elect after losing employment.
• Account can be used to fund insurance premiums only and can also include reimbursement for qualified medical expenses not covered by the health insurance plan.	• Premiums are dedicated to employer-sponsored benefits and there is no reimbursement for qualified medical expenses not covered by the health insurance plan.

Source: Jeff Rubleski

[4] Federal Register, https://www.federalregister.gov/documents/2017/10/17/2017-22677/promoting-healthcare-choice-and-competition-across-the-united-states

[5] IRS Notice 2002-45 & Revenue Ruling 2002-41 application for use referenced in Notice 2013-54; https://www.irs.gov/pub/irs-drop/n-13-54.pdf

An ICHRA functions as a health reimbursement arrangement
HRAs have been used by organizations dating back to the 1960s to compensate employees for medical expenses that were not covered by traditional health insurance plans. They were formally defined by the IRS on June 26, 2002, through IRS Notice 2002-45 and Revenue Ruling 2002-41.[5] These IRS decisions provided rules specifying how HRAs could be used to enjoy tax-deductible status for employer funding and tax-free status for employee use of the funds paid through the HRA to compensate employees for qualified medical expenses. The central requirement for all HRAs is that the employer is responsible for 100% funding of specified HRA benefits. The employer has considerable latitude with how the HRA will reimburse employees for qualified medical expenses, making the HRA a popular option for employers of all sizes. An ICHRA follows the HRA guidelines and functions as a health reimbursement arrangement with added flexibility granted by federal regulation.

An ICHRA is not a health insurance plan
The ICHRA requires 100% employer funding and gives employers added flexibility by allowing employers to designate tax-free employee reimbursement from the ICHRA for the employee's purchase of individual policy health insurance coverage. It also allows the same flexibility of the traditional HRA by permitting employers to allow reimbursement of qualified medical expenses from the ICHRA for such expenses as health plan deductibles, co-payments, co-insurance, dental and vision expenses, and a host of other qualified medical expenses. With an ICHRA in place, the eligible employee purchases an individual coverage health policy from any health insurance carrier offering qualified coverage to individuals and their dependents and then receives tax-free reimbursement from the ICHRA established by the employer. Bottom line, ICHRAs provide employers with a potent new funding mechanism to permit the use of tax-deductible employer contributions to allow employees that purchase individual health insurance to receive tax-free reimbursement to pay for individual market health insurance premiums.

Will ICHRAs be implemented by a significant number of employers moving forward?
Only time will tell if this relatively new option available for employers to fund employee-purchased health insurance premiums and qualified medical expenses will gain traction with employers. Since ICHRAs became effective starting January 1, 2020, and with the impact COVID-19 has had in slowing the economy since early 2020, most businesses and their health insurance advisors have limited knowledge of the unique characteristics of the ICHRA and its application for employers. It is unlikely that employers with established employer-sponsored health benefits will consider adopting an ICHRA for some time as it would end the employer's sponsorship of group coverage and create disruption with existing covered employees who are used to receiving health insurance coverage provided by their employer. However, for businesses that do not provide health insurance coverage — about 70% of all small businesses with fewer than 50 employees in Michigan — the ICHRA is worth investigating as a new benefit that helps to retain and attract employee talent.

For more information about ICHRAs, businesses should turn to their health insurance advisor or seek the counsel of a qualified health insurance agent. Qualified health insurance agents can be located through the National Association of Health Underwriters, **www.nahu.org.** ■